EXECUTIVE SECRETARIAT
ROUTING SLIP

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Remarks

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Executive Secretary

10 Aug 85
Date

3637 (10-81)

THE WHITE HOUSE
WASHINGTON

August 7, 1985

NOTE FOR WILLIAM J. CASEY

FROM: ROGER B. PORTER RBP

The minutes of the Economic Policy Council for July 30, 31 and August 1, 1985 are attached.

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MINUTES
ECONOMIC POLICY COUNCIL

July 30, 1985
2:00 p.m.
Roosevelt Room

Attendees: Messrs. Baker, Block, Baldrige, Brock, Yeutter, Sprinkel, McFarlane, Whitehead, Burnley, Wright, Kingon, McAllister, Oglesby, Rollins, Speakes, Daniels, Holmer, Khedouri, Mulford, Naylor, Niehenke, Stucky, Sigur, and Wallis.

1. Japanese Action Plan for Imports

Secretary Baker stated that earlier in the day the White House Office of the Press Secretary issued a preliminary statement on the Japanese Action Plan for Imports that indicated that the Economic Policy Council would begin a thorough examination and analysis of the plan. He asked that the Council consider whether an additional, more detailed statement was necessary. Mr. Speakes explained that the White House press release stated that the Administration would reserve final judgement on the Plan until its effect on U.S. exports is realized.

Several members of the Council stressed a distinction between what the Administration says publicly and what the Administration privately conveys to the Japanese Government. A number of Council members, while noting some encouraging elements of the Action Plan, expressed a general frustration with the lack of specific measures and the three year timetable for implementation, which is believed to be too long. Some members expressed disappointment that the Action Plan did not include specific measures to encourage greater Japanese imports of high technology, and agricultural and wood products.

The Council agreed that the Action Plan proposals for expediting the standards and certification process, including accepting foreign test data, were encouraging. The effectiveness of the new procedures however, cannot be determined immediately because it depends entirely on how the Japanese bureaucracy implements the new procedures. The Action Plan promise of an on-going high-level review was seen as encouraging.

The Council also noted that the Action Plan promises significant and immediate opening of the Japanese capital markets.

Decision

Secretary Baker summarized the public position on the Action Plan agreed upon by the Council:

1. The Plan is a step in the right direction.

2. We are pleased with the progress in opening up the Japanese capital markets.

3. We are concerned that three years may be too long an implementation period.

4. We reserve judgement on the effectiveness of the plan until it is implemented.

5. We will continue to work with the Japanese to open their domestic markets to U.S. exports.

The Council also established a working group to begin developing a private response to the Japanese Government.

2. Agricultural Credit Policy

Undersecretary Naylor reported that, although the Farm Credit System (FCS) is fiscally sound, some elements of the system, particularly the short-term lending operations in the Federal Intermediate Credit Banks (FICB) are facing severe financial difficulties. The strength of the overall system is evidenced by its liquidity. Of the $13 billion in stock, retained earnings, and loss allowances, the FCS has $4 billion to $6 billion in relatively liquid assets, and also holds about $500 million to $1 billion of unused short-term lines of credit.

He noted however that there are several problem FICB districts, with the Omaha district, covering Nebraska and Iowa, under particular stress. To overcome the drain of non-performing loans, these district banks are raising interest rates, at a time when interest rates in general are falling. The result of rising FICB interest rates is that good customers search for other sources of credit, leaving the poorer quality loans left as FICB assets.

Mr. Naylor explained that despite the overall strength of FCS, there are two major barriers to the system addressing its own problem. First, the system is highly decentralized and operates on a consensus management basis. Because the

FCS's equity is spread among 900 separate entities and these entities are required to share losses only if there is a technical default, districts requiring additional equity to stabilize operations cannot easily draw on the reserves of other districts. Second, the Farm Credit Administration (FCA), which supervises the farm credit system, lacks the regulatory authority and enforcement powers to require acceptable credit standards. A test of the system's ability to resolve its problems will come in August, when the districts vote whether to provide the Omaha bank $435 million in assistance.

He explained that the Working Group on Agricultural Credit Policy established three policy objectives for addressing farm credit issues:

1. Establishing a framework in which the flow of credit into the agricultural sector eventually conforms more closely with the market allocation of credit.

2. Minimizing the short-and long-term budget costs of any solution.

3. Ensuring that any credit solution is consistent with our overall agricultural policy.

Mr. Naylor outlined three options developed by the Working Group for the Council's consideration:

1. Encourage the FCS to solve its problems without Federal aid or interference.

2. Require the FCS to utilize its internal resources and restructure the FCA to provide it strong regulatory authority, enforcement powers, and Federal oversight. In exchange for these actions, the Federal Government would provide a line of credit over and above the current $250 million or direct Federal financing for FCS from the Treasury.

3. Require the FCS to utilize its internal resources and restructure the FCA to provide it strong regulatory authority, enforcement powers, and Federal oversight. In exchange for these actions, the Federal Government would create a Federally-chartered, partially Federally guaranteed, and privately owned credit institution (Aggie Mae) to purchase nonperforming loans from any recognized financial institution.

Mr. Naylor noted that both options 2 and 3 could expose the Federal Government to costs of $10 billion to $30 billion over the next three to four years.

Decision

The Council unanimously agreed to recommend option 1, encouraging the FCS to solve its problems without Federal aid or interference. The Council also agreed that further discussion or study of options 2 or 3 would be undesirable because it would raise in some minds the possibility of Federal assistance and discourage the FCS from addressing its problems.